BEFORE THE
PUBLIC SERVICE COMMISSION OF
SOUTH CAROLINA

DOCKET NO. 2015-1-E

In the Matter of	)	
Annual Review of Base Rates	)	**DIRECT TESTIMONY OF**
For Fuel Costs for	)	**KENNETH D. CHURCH FOR**
Duke Energy Progress, Inc.	)	**DUKE ENERGY PROGRESS, INC.**
	)	

Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

A. My name is Kenneth D. Church and my business address is 526 South Church Street, Charlotte, North Carolina.

Q. BY WHOM ARE YOU EMPLOYED AND IN WHAT CAPACITY?

A. I am the Manager of Nuclear Fuel Engineering's Fuel Management & Design for Duke Energy Progress, Inc. ("DEP" or the "Company") and Duke Energy Carolinas, LLC ("DEC").

Q. WHAT ARE YOUR PRESENT RESPONSIBILITIES AT DEP?

A. I am responsible for nuclear fuel procurement and spent fuel management, as well as the fuel mechanical design and reload licensing analysis for the nuclear units owned and operated by DEP and DEC.

Q. PLEASE SUMMARIZE YOUR EDUCATIONAL BACKGROUND AND PROFESSIONAL EXPERIENCE.

A. I graduated from North Carolina State University with a Bachelor of Science degree in mechanical engineering. I began my career with DEC in 1991 as an engineer and worked in various roles, including nuclear fuel assembly and control component design, fuel performance, and fuel reload engineering. I assumed the commercial responsibility for purchasing uranium, conversion services, enrichment services, and fuel fabrication services at DEC in 2001. Beginning in 2011, I incrementally assumed responsibility at DEC for spent nuclear fuel management along with the nuclear fuel mechanical design and reload licensing analysis functions. Subsequently, I assumed the same responsibilities for DEP following the merger between Duke Energy Corporation and Progress Energy, Inc.

I have served as Chairman of the Nuclear Energy Institute's Utility Fuel Committee, an association aimed at improving the economics and reliability of nuclear fuel supply and use, and I am currently a registered professional engineer in the state of North Carolina.

Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY IN THIS PROCEEDING?

A. The purpose of my testimony is to (1) provide information regarding DEP's nuclear fuel purchasing practices, (2) provide costs for the March 1, 2014 through February 28, 2015 review period ("review period"), and (3) describe changes forthcoming for the July 1, 2015 through June 30, 2016 billing period ("billing period").

Q. YOUR TESTIMONY INCLUDES TWO EXHIBITS. WERE THESE EXHIBITS PREPARED BY YOU OR AT YOUR DIRECTION AND UNDER YOUR SUPERVISION?

A. Yes. These exhibits were prepared at my direction and under my supervision, and consist of Church Exhibit 1, which is a Graphical Representation of the Nuclear Fuel Cycle, and Church Exhibit 2, which sets forth the Company's Nuclear Fuel Procurement Practices.

Q. PLEASE DESCRIBE THE COMPONENTS THAT MAKE UP NUCLEAR FUEL.

A. In order to prepare uranium for use in a nuclear reactor, it must be processed from an ore to a ceramic fuel pellet. This process is commonly broken into four distinct industrial stages: (1) mining and milling, (2) conversion, (3) enrichment, and (4) fabrication. This process is illustrated graphically in Church Exhibit 1.

Uranium is often mined by either surface (i.e., open cut) or underground mining techniques, depending on the depth of the ore deposit. The ore is then sent to a mill where it is crushed and ground-up before the uranium is extracted by leaching, the process in which either a strong acid or alkaline solution is used to dissolve the uranium. Once dried, the uranium oxide (“U_3O_8”) concentrate – often referred to as yellowcake – is packed in drums for transport to a conversion facility. Alternatively, uranium may be mined by in situ leach (“ISL”) in which oxygenated groundwater is circulated through a very porous ore body to dissolve the uranium and bring it to the surface. ISL may also use slightly acidic or alkaline solutions to keep the uranium in solution. The uranium is then recovered from the solution in a mill to produce U_3O_8.

After milling, the U_3O_8 must be chemically converted into uranium hexafluoride (“UF_6”). This intermediate stage is known as conversion and produces the feedstock required in the isotopic separation process.

Naturally occurring uranium primarily consists of two isotopes, 0.7% Uranium-235 (“U-235”) and 99.3% Uranium-238 (“U-238”). Most of this country’s nuclear reactors (including those of the Company) require U-235 concentrations in the 3-5% range to operate a complete cycle of 18 to 24 months between refueling outages. The process of increasing the concentration of U-235 is known as enrichment. Gas centrifuge is the primary technology used by the commercial enrichment suppliers. This process first applies heat to the UF_6 to create a gas, then, using the mass differences between the uranium isotopes, the natural uranium is separated into two gas streams, one being enriched to the desired level of U-235, known as low enriched uranium, and the other being depleted in U-235, known as tails.

Once the UF_6 is enriched to the desired level, it is converted to uranium dioxide ("UO_2") powder and formed into pellets. This process and subsequent steps of inserting the fuel pellets into fuel rods and bundling the rods into fuel assemblies for use in nuclear reactors is referred to as fabrication.

Q. PLEASE PROVIDE A SUMMARY OF DEP'S NUCLEAR FUEL PROCUREMENT PRACTICES.

A. As set forth in Church Exhibit 2, DEP's nuclear fuel procurement practices involve computing near and long-term consumption forecasts, establishing nuclear system inventory levels, projecting required annual fuel purchases, requesting proposals from qualified suppliers, negotiating a portfolio of long-term contracts from diverse sources of supply, and monitoring deliveries against contract commitments.

For uranium concentrates, conversion, and enrichment services, long-term contracts are used extensively in the industry to cover forward requirements and ensure security of supply. Throughout the industry, the initial delivery under new long-term contracts commonly occurs several years after contract execution. DEP relies extensively on long-term contracts to cover the largest portion of its forward requirements. By staggering long-term contracts over time for these components of the nuclear fuel cycle, DEP's purchases within a given year consist of a blend of contract prices negotiated at many different periods in the markets, which has the effect of smoothing out DEP's exposure to price volatility. Diversifying fuel suppliers reduces DEP's exposure to possible disruptions from any single source of supply. Due to the technical complexities of changing fabrication services suppliers, DEP generally sources these services to a single domestic supplier on a plant-by-plant basis using multi-year contracts.

Q. PLEASE DESCRIBE DEP'S DELIVERED COST OF NUCLEAR FUEL DURING THE REVIEW PERIOD.

A. Staggering long-term contracts over time for each of the components of the nuclear fuel cycle means DEP's purchases within a given year consist of a blend of contract prices negotiated at many different periods in the markets. DEP mitigates the impact of market volatility on the portfolio of supply contracts by using a mixture of pricing mechanisms. Consistent with its portfolio approach to contracting, DEP entered into several long-term contracts during the review period.

DEP's portfolio of diversified contract pricing yielded an average unit cost of $40.77 per pound for uranium concentrates during the review period, representing a decrease of 17% per pound from the prior review period. This decrease can be attributed to implementation of the merged nuclear fleet procurement strategy and the availability of low priced uranium market opportunities.

A majority of DEP's enrichment purchases during the review period were delivered under long-term contracts negotiated prior to the review period. The staggered portfolio approach has the effect of smoothing out DEP's exposure to price volatility. The average unit cost of DEP's purchases of enrichment services during the review period increased 5% to $134 per Separative Work Unit.

Delivered costs for fabrication services generally trended upward during the review period, consistent with escalation in material and labor costs, while delivered conversion services costs remained relatively flat during the review period. These costs, however, have a limited impact on the overall fuel expense rate given that the dollar amounts for these purchases represent a substantially smaller percentage – 13% and 4%, respectively, for the fuel batches recently loaded into DEP's reactors – of DEP's total direct fuel cost relative to uranium concentrates or enrichment, which are 45% and 38%, respectively.

Q. PLEASE DESCRIBE THE LATEST TRENDS IN NUCLEAR FUEL MARKET CONDITIONS.

A. Prices in the uranium concentrate markets remain relatively low with the continued lack of demand due to the event at Fukushima. Industry consultants, however, believe market prices need to increase from current levels in order to provide the economic incentive for the exploration, mine construction, and production necessary to support future industry uranium requirements.

Market prices for enrichment services have declined primarily due to reduced demand following the Fukushima event. Additionally, the transition by enrichment suppliers from gaseous diffusion technology to the more cost efficient gas centrifuge technology was a market driver.

Fabrication is not a commodity for which prices are published; however, industry consultants expect fabrication prices will continue to generally trend upward. For conversion services, market prices remained relatively stable during the review period.

Q. WHAT CHANGES DO YOU SEE IN DEP'S NUCLEAR FUEL COST IN THE BILLING PERIOD?

A. The Company anticipates a decrease in nuclear fuel costs on a cents per kilowatt hour ("kWh") basis through the next billing period. Because fuel is typically expensed over two to three operating cycles – roughly three to six years – DEP's nuclear fuel expense in the upcoming billing period will be determined by the cost of fuel assemblies loaded into the reactors during the review period, as well as prior periods. The fuel residing in the reactors during the billing period will have been obtained under historical contracts negotiated in various market conditions. Each of these contracts contribute to a portion of the uranium, conversion, enrichment, and fabrication costs reflected in the total fuel expense.

The average fuel expense is expected to decrease from 0.688 cents per kWh incurred in the review period, to approximately 0.661 cents per kWh in the billing period. This expected decrease is primarily attributed to the reduction of Department of Energy waste fee collections to zero.

Q. WHAT STEPS IS DEP TAKING TO PROVIDE STABILITY IN ITS NUCLEAR FUEL COSTS AND TO MITIGATE PRICE INCREASES IN THE VARIOUS COMPONENTS OF NUCLEAR FUEL?

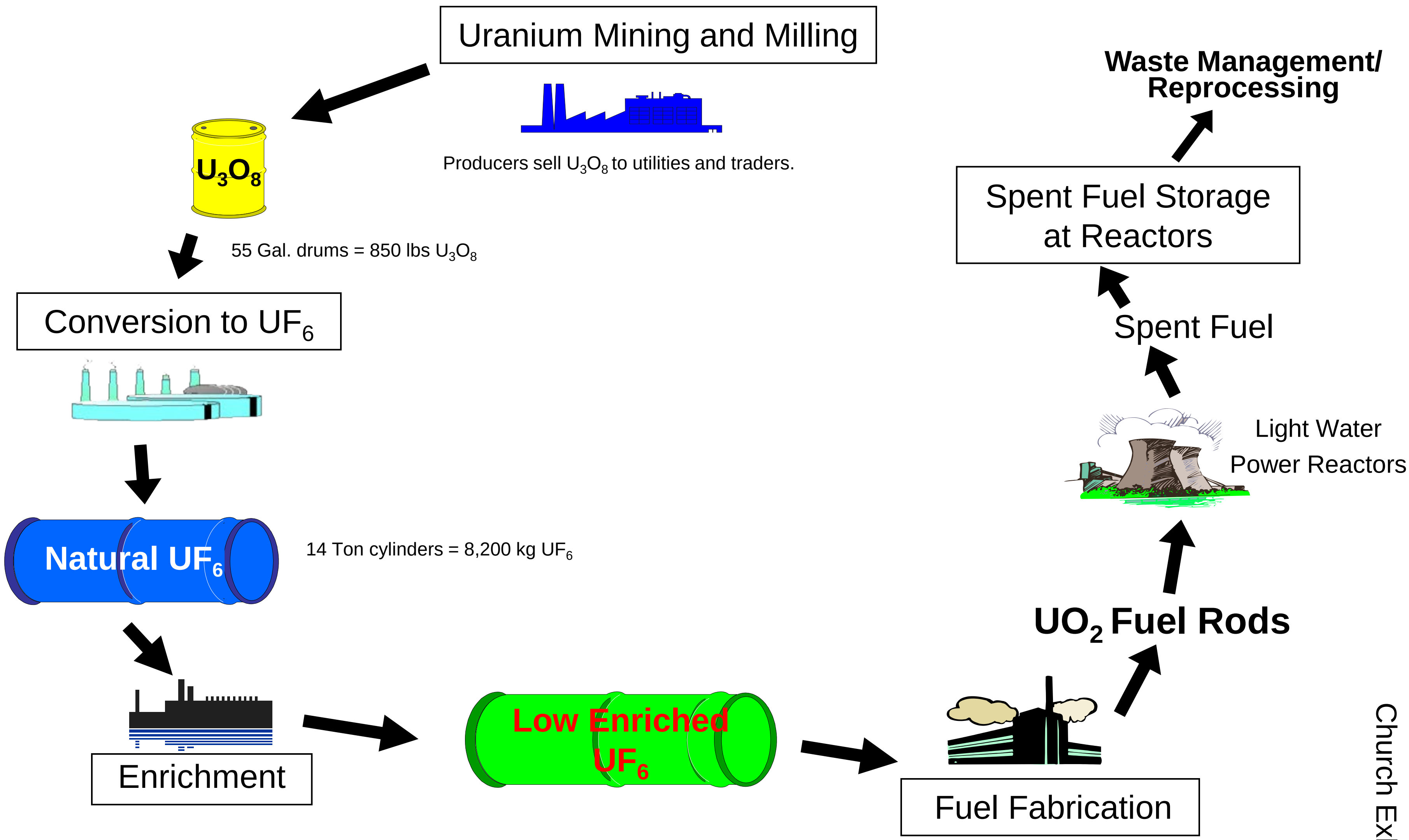
A. As I discussed earlier and as described in Church Exhibit 2, for uranium concentrates, conversion, and enrichment services, DEP relies extensively on staggered long-term contracts to cover the largest portion of its forward requirements. By staggering long-term contracts over time and incorporating a range of pricing mechanisms, DEP's purchases within a given year consist of a blend of contract prices negotiated at many different periods in the markets, which has the effect of smoothing out DEP's exposure to price volatility.

Although costs of certain components of nuclear fuel are expected to increase in future years, nuclear fuel costs on a cents per kWh basis will likely continue to be a fraction of the cents per kWh cost of fossil fuel. Therefore, customers will continue to benefit from DEP's diverse generation mix and the strong performance of its nuclear fleet through lower fuel costs than would otherwise result absent the significant contribution of nuclear generation to meeting customers' demands.

Q. DOES THIS CONCLUDE YOUR PRE-FILED DIRECT TESTIMONY?

A. Yes, it does.

The Nuclear Fuel Cycle



Church Exhibit 1

Church Exhibit 2

Duke Energy Progress Nuclear Fuel Procurement Practices

The Company's nuclear fuel procurement practices are summarized below.

- Near and long-term consumption forecasts are computed based on factors such as: nuclear system operational projections given fleet outage/maintenance schedules, adequate fuel cycle design margins to key safety licensing limitations, and economic tradeoffs between required volumes of uranium and enrichment necessary to produce the required volume of enriched uranium.
- Nuclear system inventory targets are determined and designed to provide: reliability, insulation from market volatility, and sensitivity to evolving market conditions. Inventories are monitored on an ongoing basis.
- On an ongoing basis, existing purchase commitments are compared with consumption and inventory requirements to ascertain additional needs.
- Qualified suppliers are invited to make proposals to satisfy additional or future contract needs.
- Contracts are awarded based on the most attractive evaluated offer, considering factors such as price, reliability, flexibility and supply source diversification/portfolio security of supply.
- For uranium concentrates, conversion and enrichment services, long term supply contracts are relied upon to fulfill the largest portion of forward requirements. By staggering long-term contracts over time, the Company's purchases within a given year consist of a blend of contract prices negotiated at many different periods in the markets, which has the effect of smoothing out the Company's exposure to price volatility. Due to the technical complexities of changing suppliers, fabrication services are generally sourced to a single domestic supplier on a plant-by-plant basis using multi-year contracts.
- Spot market opportunities are evaluated from time to time to supplement long-term contract supplies as appropriate based on comparison to other supply options.
- Delivered volumes of nuclear fuel products and services are monitored against contract commitments. The quality and volume of deliveries are confirmed by the delivery facility to which Duke Energy Progress has instructed delivery. Payments for such delivered volumes are made after Duke Energy Progress' receipt of such delivery facility confirmations.